



**Interim Economic Affairs Committee**

**February 7, 2008**



## Montana State Fund

Who we are:

- Workers' Compensation insurance is mandatory for employers
- Montana State Fund;
  - Provides a competitive option for an employer to purchase workers' compensation insurance for their employees
  - Serves as the *guaranteed market* for Montana employers to purchase workers' compensation insurance



## State Fund Structure

### Four States - Monopolistic State Funds

Wyoming	North Dakota
Washington	Ohio

### Fourteen States - Competitive/Guaranteed Market

California	<u>Montana</u>
Colorado	New York
Hawaii	Oklahoma
Kentucky	Pennsylvania
Louisiana	Rhode Island
Maine	Texas
Maryland	Utah

### Eight States - Competitive/NOT Guaranteed Market

Arizona	Missouri
Idaho	New Mexico
Minnesota	Oregon
West Virginia	South Carolina (Public Agencies Only)



## Montana State Fund

Approximately 28,000 Active Policies

Claims from Injured Employees:

- Reported in FY 2007: 15,103
- Currently Open: 8,381



## Montana State Fund

Estimated Portion of Market\*

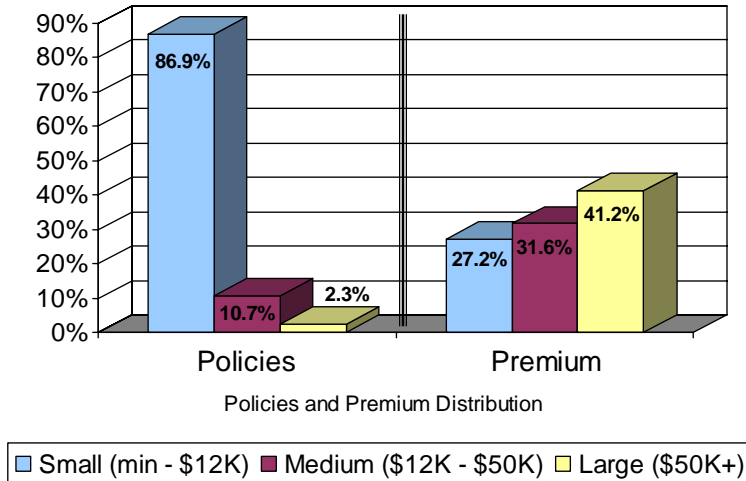
- Montana (Estimated)
  - Insured Market (2006)
    - MSF – 68%
    - Private Carriers – 32%
- National Market – 0.6%

\* Does not include Montana Self-Insured Employers



## Montana State Fund

### Policy and Premium Distribution by Size of Account



## Management of Montana State Fund

WHY DID THE LEGISLATURE CREATE MONTANA STATE FUND AS A NON-PROFIT INDEPENDENT PUBLIC CORPORATION?

- To ensure the State Fund operated similar to a domestic mutual insurance company
- To prevent the circumstances that led to the \$500 million unfunded liability for accidents occurring prior to July 1, 1990 ("Old Fund")
- To ensure long-term financial strength and solvency of MSF
- To enable Montana employers to obtain competitive workers' compensation coverage at a reasonable cost
- To maintain appropriate legislative oversight of Montana State Fund



## **Montana State Fund** **Legislative Action**

### **Legislative actions to strengthen Montana State Fund since 1989 have yielded positive results:**

- MSF is organizationally and operationally structured much like a private carrier to meet insurance business needs.
- A 7 member board of directors appointed by the Governor
  - Responsibility for:
    - Rates
    - Establishing Equity (Surplus) Level
    - Declaring Dividends, if any
    - Annual Budget
    - Annual Strategic Business Plan
    - Annual Financial Report



### **WHAT TYPE OF LEGISLATIVE OVERSIGHT EXISTS ?**

- MSF's Seven Member Board of Directors Appointed by Governor (2-15-1019, MCA)
- Annual Legislative Audit of Loss Reserves and Financial Statements (39-71-2361, MCA)
  - ❖Independent Actuary (LAD) review of Rates (39-71-2362, MCA)
- Two Legislative Liaisons Appointed from Economic Affairs Committee (2-15-1019, MCA)
- Budget Reviewed by Legislative Finance Committee (39-71-2363, MCA)
- MSF Subject to Open Meeting and Public Document Laws (2-3-203 and 2-6-101, MCA)



**Legislative actions to strengthen Montana State Fund since 1989 have yielded positive results:**

Rates are reviewed annually by the Legislative Audit Division to determine if rates are excessive, inadequate or unfairly discriminatory- the same standard as applied to **private** carriers. Also review Loss Reserves in Financial Statements.

Appropriate levels of reserves and equity (surplus) are achieved through responsible insurance operations.

These actions have and will continue to guard against the reoccurrence of the circumstances that led to the Old Fund- unfunded liability which required legislative intervention with a payroll tax.



**Financial Strength and Stability**

MSF, as a workers' compensation state fund, has several characteristics that highlight the importance of equity to absorb adverse scenarios:

- Extremely long-term obligations associated with workers' compensation claims.
- MSF writes one line of highly regulated insurance.
- MSF writes coverage in a single state.
- MSF provides a guaranteed market.
- Unlike a stockholder-owned insurance company, MSF cannot access additional capital to finance future growth or to cover adverse financial results.
- MSF's equity must be adequate not only to cover current and next year's obligations, but also to support the long-term strategy.



## Financial Strength and Stability

“MSF’s equity has done its job extremely well in recent years:

- Absorbed unprofitable years (FYs 2003 and 2004).
- Absorbed adverse loss and LAE reserve development.
- Absorbed retroactive benefit changes reflected in court decisions.
- Absorbed volatile investment climate.
- **Allowed relatively stable rates”**

*Source: Consulting Actuary Report to the Board of Directors, March 23, 2007*



## MSF Rate Actions

<u>July 1st of:</u>	<u>MSF Rates</u>
1996	-15.4%
1997	-5.6%
1998	-3.0%
1999	-2.0%
2000	0.0%
2001	2.7%
2002	2.8%
2003	11.6%
2004	9.5%
2005	3.0%
2006	2.4%
2007	-1.0%



## Premium Rates Charged to Customers



### How Insurance Companies Establish Rates

- NCCI (National Council on Compensation Insurance) files loss-costs by class code
- Insurance Commissioner has 30 days to disapprove (file and use)
- Insurers file Loss Cost Multiplier (LCM)





## Loss-Costs vs. Manual Rates

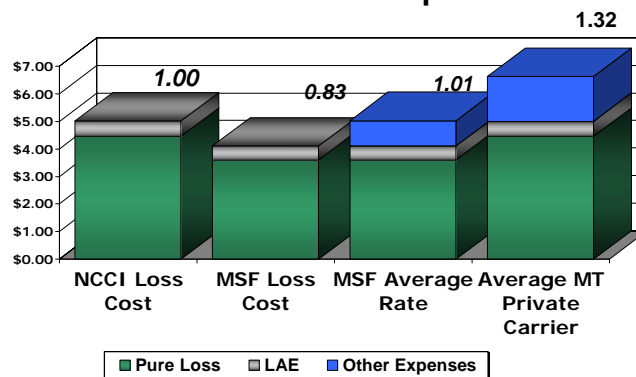
Loss Costs = claim benefits + claim administrative expense

Loss Cost Multiplier (LCM) =  
+ general/production expense  
+/- underwriting offsets  
+ taxes and assessments  
+ contingencies, profit, & investment offsets

Rates = Loss Costs x Loss Cost Multiplier (LCM)

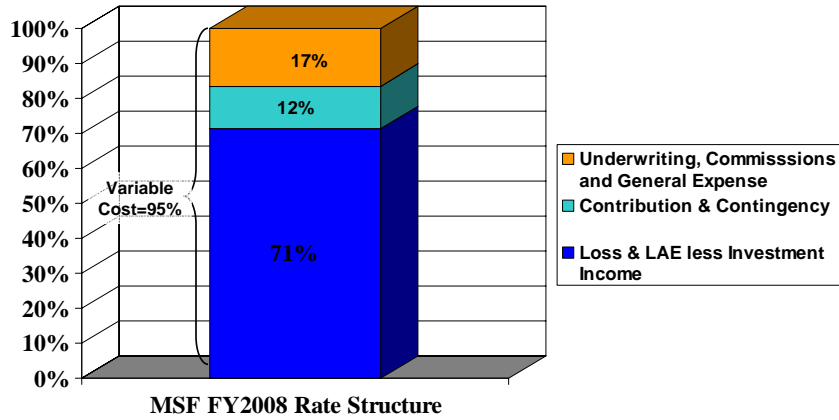


### NCCI Loss Costs Compared to MSF Rate





## What Makes up the MSF Rate



### Statutory Expense Ratio Excluding Dividends - MSF

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Target	26.20%	25.80%	26.4%	29.0%	28.4%
Actual		27.3%	25.4%	22.1%	25.6%

### Average Expense Ratio - Top 10 Carriers - Excluding Dividends

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Actual	n/a	n/a	40.0%	39.2%	38.9%

Note 2: 2006 is most current year for which data is available on 8 of the Top 10 carriers ratios for MT Workers Comp carriers. 2005 is most current data on 2 of the carriers.

Note 3: Top 10 Carriers high expense ratio was 43.9% and low expense ratio was 31.9%.



## State Agency Program

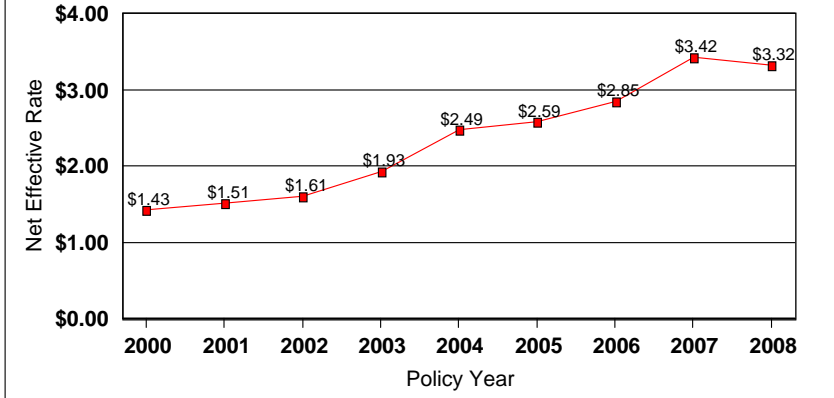


## State Agency Program

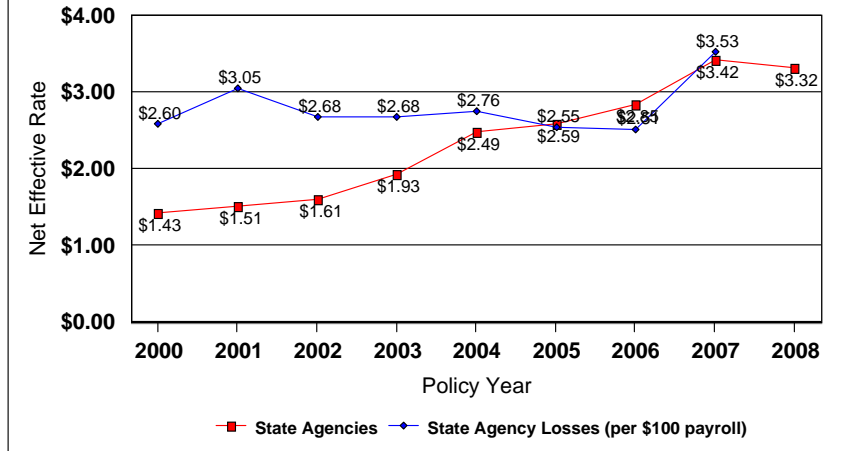
- Number of Agency Policies - 37
- Premium Volume Estimated FY 2008 - \$17.7 M.
- Largest Agencies (68% of Premium)
  - DPHHS
  - Transportation
  - Corrections
- Top Ten Agencies are 90% of Premium
  - (Justice, Labor, DNRC, FWP, Revenue, Administration, MSF)
- Captive
- State agency experience drives their rates as MSF assigns unique class codes and provides underwriting programs that can return premiums



### State Agencies Net Effective Rate



### State Agency Rate vs State Agency Loss Costs





## Old Fund



## Old Fund Statutes

### **Section 39-71-2351, MCA**

#### **Separation of Old Fund liability separate funding of claims for the Old Fund and the State Fund (New Fund).**

- The legislature has determined that the most cost-effective and efficient way to provide a source of funding for and to ensure payment of the unfunded liability and the best way to administer the unfunded liability is to separate the liability of the state fund on the basis of whether a claim is for an injury resulting from an accident that occurred before July 1, 1990, or an accident that occurs on or after that date.



## Old Fund Statutes

### **Section 39-71-2352, MCA**

#### **Separate payment structure and sources for claims for injuries of the Old Fund and the State Fund (New Fund)**

- Premiums paid to the Old Fund may be used ***only*** to administer/pay claims of the Old Fund.
- Premiums paid to the state fund (New Fund) may be used ***only*** to administer/pay claims of the New Fund.
- Determine the cost to administer/pay claims of the Old Fund and separately determine the cost to administer/pay claims of the New Fund.
- Fund administrative expenses and benefit payments for the Old Fund the New Fund separately from the sources provided by law.



## Old Fund Statutes

### **Section 39-71-2352, MCA (Continued)**

- The independent actuary of the state fund will project the unpaid claims liability of the Old Fund.
- If in any fiscal year, claims are not "adequately funded", funds must be transferred from the General Fund to the Old Fund
- "Adequately funded" means the present value of:
  - (a) the total cost of future benefits remaining to be paid; and
  - (b) the cost of administering the claims."

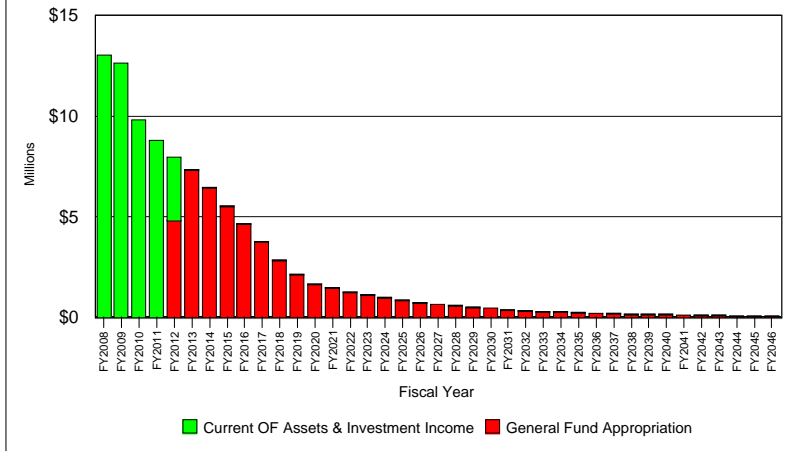


## FY 2007 Old Fund Balance Sheet As Of June 30, 2007

Old Fund	FY 2007	FY 2006
<b>Assets:</b>		
Invested Assets	\$ 42,575	\$ 51,928
Other Assets	14,262	15,574
<b>Liabilities:</b>		
Loss Reserves	\$ 75,063	\$ 73,736
Other Liabilites	14,408	15,667
<b><u>Net Assets</u></b>	<b><u>\$ (32,634)</u></b>	<b><u>\$ (21,901)</u></b>



### Old Fund Annual Expenditures By Funding Source





## What is Keeping Us up Late At Night



## Court Decisions

### Impact on Volatility of Results

For example:

- Stavenjord – Statute held unconstitutional retroactive to 1987
- Schmill – Common Fund – Statute held unconstitutional retroactive to 1987





## Impacts of Court Decisions

### **Satterlee (Not in Loss Reserves)**

Challenges 39-71-710, MCA, passed by the Legislature in 1981, authorizes termination of permanent total disability benefits and rehabilitation benefits when a claimant receives or becomes eligible to receive full Social Security retirement benefits or an alternative to that plan. Should the statute be found to be unconstitutional as applied to permanent total benefits, *Satterlee, et al.* request [payment of lifetime permanent total disability benefits](#). Also requests certification of this case as a [class action or as a common fund](#) for similarly situated claimants.

### **Cost Estimates (if unconstitutional and applied retroactively)**

New Fund – (non-settled claims arising on or after July 1, 1990 through December 22, 2004) - \$135 million to \$186 million.

Old Fund - \$93 to \$116 million.

### **Status**

Workers' Compensation Court held statute constitutional. Supreme Court appeal dismissed on procedural grounds. Pending again before the Workers' Compensation Court